The Full Employment Project

The Center on Budget and Policy Priorities launched its Full Employment Project in April 2014, with a conference at the National Press Club at which leading analysts representing a variety of political perspectives presented a series of papers on full-employment issues. The papers have provoked discussion in policy and academic circles and attracted significant media coverage.

The Project now seeks to move into full operation (and to attract philanthropic support to do so). Moving forward, the Project's work will focus on three related policy goals:

- *Getting to full employment,* both by 1) reducing the depth, length, and adverse effects of recessions, — especially their impact on jobs — by securing more effective stabilization policies; and 2) spurring more robust job creation in economic recoveries so that the economy is more often at or near full employment. The benefits of full employment, in terms of wages and living standards, are most helpful to low- and modest-wage workers.

- *Setting a policy agenda for the next recession*: This goal is closely related to the one above. Despite various shortcomings, the safety net and monetary and fiscal policy generally were effective in preventing the Great Recession from becoming an even more severe downturn. This point is not sufficiently appreciated, however, and that risks leaving the nation unprepared for effective responses to the next downturn. As part of the Project, we will review the effectiveness of various measures taken in response to the recession and propose ways to develop effective responses to the next recession.

- *Repairing ongoing damage from the Great Recession, such as the decline in labor force participation, and improving workers' skills* — and thereby raising "potential GDP" (i.e., the size of the economy at full employment). A larger full-employment economy produces higher incomes.

Producing quality analyses and developing and advancing promising policy ideas will not, however, be sufficient by themselves. Making substantial progress also entails engaging vigorously in debates on these issues in the public sphere and "winning the argument," as Project director Jared Bernstein puts it. As a result, the Project also has a communications component focused on the public debate on these issues. Both the policy component and the communications component of the Project are described below.

As noted, the Project will be led by Jared Bernstein, who will devote the majority of his time to it over the next 2½ years. (The Project work described here would be conducted between this fall and the end of 2016.) The Center's chief economist, Chad Stone, will be substantially involved as well, devoting 25% of his time to the Project. Bernstein and Stone are significant figures in the macroeconomic policy world. Bernstein, now a Senior Fellow at CBPP, was the former top economic advisor to Vice President Biden and before that, a senior fellow at the Economic Policy Institute. He appears frequently on television, produces his own widely read blog ("On the Economy"), and is a regular contributor to "The Upshot" in the *New York Times*. Chad Stone was the chief economist for the President's Council of Economic Advisers under President Clinton and then acting executive director and chief economist, for the Congressional Joint Economic Committee. He writes a weekly column on economic policy for *U.S. News and World Report.*

I. The Project's Policy Component: The Context

Full employment — and appropriate policies to lessen declines in employment when the economy weakens and to strengthen job creation when the economy recovers — is extremely important but has become increasingly difficult to achieve in recent decades. Weak employment performance has been one of the most damaging aspects of the economy in recent years, and the unemployment rate has spent more time significantly above full employment after recent economic downturns than in earlier decades. Moreover, there is now growing concern that the economy is stuck in "secular stagnation," with slow job growth that leaves the economy with employment levels well below those that we see when the economy is at full employment.

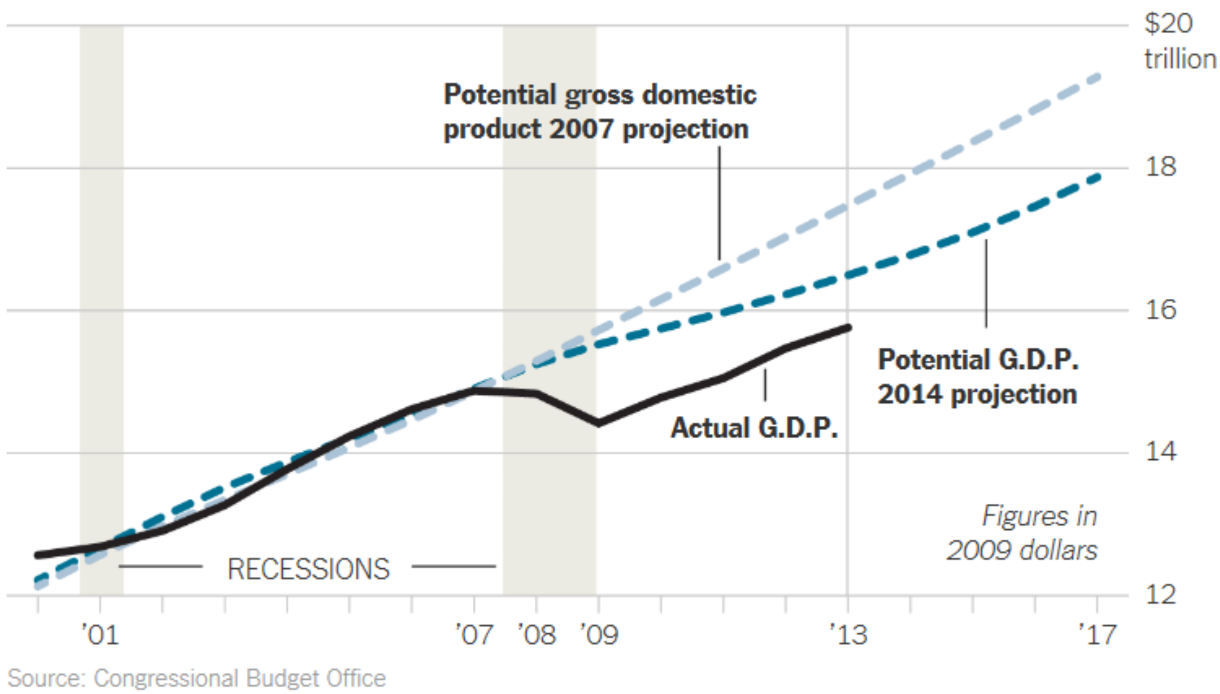
Weak labor markets create a myriad of problems. Not only do they produce high levels of unemployment and large numbers of discouraged workers who stop looking for work, but they also produce low or anemic wage growth, more inequality and poverty, and long-term damage to the career trajectories of those who began their careers in weak labor markets or have lost their jobs and subsequently remain unemployed for long stretches. Moreover, minorities and people from low-income families are typically hit the hardest.

Full employment, by contrast, not only leaves more workers with jobs but also creates an economic dynamic wherein employers must bid up wage offers to get and retain the workers they need, as we saw in the full-employment years of the latter 1990s. In this regard, one of full employment's most important attributes is that it pushes back against the long-term trend of growing wage and income inequality. Bernstein's paper, which provides an overview of the Full Employment Project (one of the papers we released in April), discusses these issues in more detail and provides empirical evidence of these critical points.

When the economy falls into a very deep recession and then remains weak for an extended period — with many people out of work for long periods — a second set of adverse developments can occur. When the economy recovers, it can emerge at a markedly smaller size than it was on track to attain before the downturn hit. To use economic terminology, "potential GDP" can take a big hit, with the result that wages and living standards in the recovered economy are significantly lower than they otherwise would have been. Moreover, given the substantial increase in inequality in recent years, these wage and job shortfalls are not equally distributed; the burden of this economic damage falls disproportionately on the least well-off.

Consider what has happened in recent years. GDP fell sharply in the Great Recession, opening a large gap between the GDP level achieved and its full-employment potential. Then, in the recovery, the economy has grown much too slowly to close the gap and restore full employment in anything close to the timeframes in which it occurred in the recoveries of earlier decades.

Moreover, larger numbers of people withdrew from the labor force due to the difficulty they encountered in finding work, less capital was invested, and productivity grew more slowly than the Congressional Budget Office (CBO) had projected before the recession. As a result, CBO has now lowered its estimate of potential economic output in 2017 by 7 percent, or about $2,500 per American. Thus, instead of making up lost ground — as in recoveries from earlier, less severe recessions — the economy has continued to grow only sluggishly *and* potential GDP has continued to fall further behind where it was expected to be. Unless these trends are reversed, they will cause a



substantial loss of wages and income for the indefinite future, relative to where forecasters' expected them to be — and where they could be under a more effective policy agenda.

Effective full-employment-oriented policies are crucial to reversing this trend in order to improve the employment prospects of millions of Americans, as well as to reduce poverty, restrain inequality, and improve wages and living conditions over time.

II. Work Ahead for the Project's Policy Component

The policy work that we propose to undertake involves both 1) examining policy areas and issues critical to full-employment goals and developing policy proposals in response; and 2) digging deeper into specific policy areas highlighted in the papers released in April, and in some cases turning concepts and ideas raised in these papers into concrete, actionable proposals for consideration by federal and state policymakers. We would do some of this work in-house; some would involve commissioning additional analysis and papers by outside experts.

We regard the seven papers developed so far as an important first step that scratched the surface. In the Project's next stage, we propose to continue developing new ideas, to flesh out various ideas, and to engage current and new outside authors as members of what we think of as "Team Full Employment" — that is, to enlist them to serve as ambassadors for these policies and the full employment goal in their regular work (that is, through their writing, public appearances, and teaching). This is an essential but often unappreciated component of building a successful economic policy agenda — enlisting other economists and policy professionals in this work, not in the atomized way in which many academics normally work but as part of a broader team and cause.

We also propose to combine the work of these outside policy conceptualizers with the granular, practical, detail-oriented work in which CBPP staff excel of taking promising policy ideas and converting them into concrete, actionable policies for policymakers to consider and advance.

The policy areas and papers for the Project's next phase include the following:

A. The Big Picture.

As the paper we released in April by Lawrence Ball, Brad DeLong, and Larry Summers explained, and as Summers' keynote address at our April conference emphasized, the economy shows signs of serious and ongoing damage from the Great Recession. The economy appears to be experiencing what economists call "hysteresis," where potential GDP, labor-force participation, business investment, and other key economic variables remain depressed on a seemingly permanent basis. We are commissioning a new paper by Ball and Summers that will explore whether well-designed fiscal and economic policies can produce "reverse hysteresis" — that is, can reverse the current "hysteresis" and bring the economy closer to its pre-recession levels of potential GDP and GDP growth.

Economists are beginning to build evidence that policies that produce much tighter labor markets would pull many of those who have left the labor market back into it. In an important new paper, economists David Blanchflower and Adam Posen have developed compelling statistical evidence suggesting that "… many individuals who are not actively searching for work under current labor stack conditions remain attached to the labor market —- a substantial portion of those American workers who because inactive should not be treated as gone forever, but should be expected to spring back into the labor market if demand rises to create jobs." Federal Reserve Chair Janet Yellen also voiced support for this concept recently, noting that "some retirements are not voluntary, and some of these workers may rejoin the labor force in a stronger economy … a significant amount of the decline in [labor force] participation in the recovery is due to slack …"

The new paper from Ball and Summers that the Project has commissioned will build on this work, advance it, and explore how appropriate policies could help reverse the hysteresis, create more jobs, and grow the economy at a stronger rate. This paper may serve as something of a foundational piece for the Project's work, and we intend to promote it to a broad audience.

B. Developing and promoting better stabilization policies to make future recessions shallower and shorter.

In 2009, President Obama and Congress enacted the American Recovery and Reinvestment Act (ARRA), one of the largest pieces of stimulus legislation on record, and analysis shows that it kept the recession from growing substantially worse. In hindsight, it's also clear that, given the depth of the downturn and the sluggishness of the ensuing recovery, ARRA was too small and ended too soon.

ARRA was distinguished from stimulus laws of earlier recessions not only by its size, but also its composition. It placed more emphasis on measures to put money directly in the pockets of low-income households — those with the greatest propensity to consume — through increases in tax credits for low-income workers, increases in SNAP (food stamp) as well as unemployment insurance (UI) benefits, jobs for low-income parents and youth, and other measures. It also placed much more emphasis on increased federal funding for states. States must balance their budgets even during recessions and, because recessions drain their revenues as people and businesses become less prosperous and pay fewer taxes, states have to make large budget cuts and/or impose tax increases to reach balance. That, in turn, makes recessions deeper and more protracted.

The role of key Recovery Act measures is not well understood— in particular, the positive efforts of the enhanced low-income assistance and state fiscal relief. Absent such understanding, policymakers will be less likely to take similar steps when the next recession hits. Yet evidence suggests that ARRA's low-income assistance and state fiscal relief components (as well as the UI components) were particularly effective in boosting the economy and saving jobs. Accordingly:

- The Project proposes to produce one or more papers on the role of the enhanced low-income and state fiscal relief measures, emphasizing their importance as high "bang-for-the-buck" counter-cyclical tools in recessions. (The Center has particular expertise in these areas. It played the lead role in designing these components of the Recovery Act in the fall of 2008, at the request of the incoming Obama Administration, and in making the case for emergency federal UI.)

- The Project also proposes to explore and develop options for strengthening the "automatic stabilizers" in the federal budget, so that more counter-cyclical measures kick in *automatically* when the economy weakens (and perhaps stay in effect until particular economic benchmarks are met). The Project will, for example, explore mechanisms for an automatic increase in the federal share of state Medicaid costs, and possibly other automatic mechanisms for federal fiscal relief or revenue-sharing with state and local governments, when the economy dips into recession. Such mechanisms would ease the severity of recessions, reducing job losses. They also would lessen or avert sharp state and local cuts in health care, education, and other important services during recessions.

- In related work, the Project would examine the potential effects that various fiscal and programmatic proposals likely to be considered in the next few years would have on the effectiveness of the "automatic stabilizers" now in place. For example, proposals to convert SNAP and Medicaid to block grants would largely remove their automatic stabilizer functions — a consideration that's not well understood. Similarly, proposals to cap federal spending at a share of GDP at or below its historical average would largely eviscerate the automatic stabilizers because in recessions, spending for things like UI, Medicaid, and SNAP automatically increases while GDP falls. Many policymakers do not sufficiently appreciate these dynamics.

- The Project could also explore *state* fiscal policies that can strengthen — or impede — economic stabilization. For example, state actions to build robust "rainy day funds" during good times — and to draw them down in recessions so that states don't have to cut spending and raise taxes as sharply — can help lessen the economic drag that state balanced-budget requirements impose during downturns. Many states do not, however, amass rainy day funds of sufficient size when times are good, and some states are reluctant to tap them when the economy sours.

- We also want to flesh out the ideas outlined in the paper by Donna Pavetti that the Project released in April. This paper explained the benefits of a subsidized employment program for low-income people who have difficulty finding jobs. The Project proposes to explore the idea of a subsidized job program that operates on a modest scale in good economic times (in part to keep its infrastructure in place) and ramps up automatically when recession threatens or sets in.

C. Taking a deeper dive, fleshing out policy concepts, and advancing them

The papers issued in April surfaced a number of promising ideas. A next step is to flesh out some of these ideas and convert them into specific, actionable policy proposals. This entails work to more fully flesh out proposals in such areas as:

- *Work sharing*: The paper from April by the American Enterprise Institute's Kevin Hassett and Michael Strain called for increased use of work-sharing, especially during economic downturns. Work-sharing can play an important role in keeping large numbers of people from joblessness for long periods, during which their skills can erode. Today, work-sharing is an *allowable* practice under the Unemployment Insurance program, but fewer than half the states use it at all. In most states that do allow it, its use is sparse. Research suggests the presence of a number of inhibiting factors. Many states view the federal rules as too difficult to comply with, and many state officials and employers are unfamiliar with this option. In short, there are both administrative barriers (some related to federal or state rules) and informational barriers. The Project could dig deeper in identifying the barriers and proposing remedies to overcome them.

- *Job training and apprenticeships*: By working with the Urban Institute's Harry Holzer and American University's Robert Lerman, the Project could seek to advance the ball in this area as well. We could commission the development of more concrete policy proposals and then work to elevate them.

- *Infrastructure*: Larry Summers has written about the multiple benefits of more investment in infrastructure: substantial job creation, which could help in reversing the economy's apparent hysteresis; improved roads, bridges, and mass transit that make the economy more efficient and productive; and lower costs in future decades for deferred maintenance. The Project could explore with Summers and/or others what next steps could advance sound policies in this area.

III. "Winning the Argument"

Many people across the political spectrum give at least lip service to their desire for full employment. But there often is confusion, misunderstanding, or disagreement about what full employment means, how far we are from it, what are the best policies to achieve it, and how to effectively stabilize the economy and grow potential GDP.

Many policymakers and journalists often assume, for example, that outside of recessionary periods, the job market is at full employment. Yet that has been more the exception than the norm over the past three decades.

In addition, good job training programs are important, but if we fail to boost employment — and we fund programs to train workers on the assumption that jobs are waiting for them when that's not so — even well-designed training programs will produce disappointing results.

Another set of issues centers on fears of inflation. Some policymakers and commentators are so worried about inflation that they argue against measures to raise aggregate demand and create jobs even when unemployment remains high and inflation remains below target levels, as is the case today.

Furthermore, some argue that only tax cuts (or only tax cuts and deregulation measures) can promote employment and all other fiscal policy measures are bound to fail or cause harm, despite ample evidence to the contrary. Even when there is agreement that some forms of direct job creation (such as the subsidized jobs programs that Pavetti's paper calls for) could create jobs, there often is still disagreement about whether such policies are desirable because they entail new federal spending.

Accordingly, the Project will seek to engage in debates on these matters and persuasively advance the policy ideas and proposals — and the analysis underlying them — that emerge from the Project's work. Thus, the Project will include substantial communications and public education work across various types of media, including social media. This work also may include forums or briefings akin to the Project's event in April.

To advance its communications and public education efforts, the Project will capitalize on Jared Bernstein's popular blog ("On the Economy"), his column in the *New York Times'* "The Upshot" section, and his extensive work on cable news stations MSNBC and CNBC. It will also capitalize on Chad Stone's weekly column in *U.S. News and World Report*, the Center's own widely read blog ("Off the Charts"), both the Full Employment Project and the Center websites, the twitter feeds of various Center staff (including CBPP President Bob Greenstein as well as Bernstein and Stone), and various other means of disseminating Project findings, ideas, and messages and engaging in debates on the issues noted above.

For example, an important near-term debate centers on how quickly the economy is approaching full employment — an issue that's especially portentous for the Federal Reserve as it conducts monetary policy. Short, accessible analytic pieces of the type that Bernstein features on his blog can be useful in this regard, especially when they enable us to hook our messages to short-term news developments, such as government data releases on jobs, inflation, and wages.

These issues have received more attention of late because the unemployment rate has fallen in recent months, leading some to urge the Federal Reserve to tighten monetary policy (as a means of preventing further inflation). The modest downward trend in the jobless rate is due in substantial part, however, to people dropping out of the labor force. Both Bernstein and Stone have expounded on this issue and will continue to do so.

Issues like these will continue to surface, in some cases on almost a daily basis. The Project will pursue them, with the goal of keeping full employment in the echo chamber of the policy debate.

In essence, "winning the argument" entails ongoing analysis of, and a communications and media presence on, these issues. It requires a steady stream of analyses, blogposts, and commentaries on the dynamics of unemployment and inflation so policymakers do not over-emphasize inflationary concerns at the expense of lower unemployment.

Similarly, the Project proposes to do more media and public education work on "hysteresis," the concept discussed above that problems emanating from the Great Recession (e.g., the decline in labor-force participation) are persisting and threaten to permanently reduce the economy's underlying growth rate. (To the extent that people who could work stay out of the labor force, the economy's potential growth rate will be lowered.)

On the Full Employment Project website, we recently posted an important piece of new work (since our April conference) by Lawrence Ball, which documents the extent of hysteresis across a number of advanced economies and suggests that, rather than being an anomaly, hysteresis is a serious and costly economic problem in many advanced economies today. In addition, as noted earlier, the Project has commissioned important new work by Summers and Ball on "reverse hysteresis" — the concept that hysteresis can be reversed. Fostering greater understanding by policymakers, journalists and other opinion-leaders that hysteresis poses a serious problem but could potentially be reversed through well-crafted full employment and related economic policies will be an important part of the Project's work.

In short, what's lacking in the public policy debate, and what this part of the Project seeks to undertake, is a continuous effort to collect and promote to wider audiences key findings and messages on these important employment and employment-related economic issues — in particular, why it's so important to return to full employment and what are some of the promising ways to get there.